

Avon Pension Fund

Panel Investment Report Quarter to 30 June 2024

August 2024

Steve Turner

A business of Marsh McLennan



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Executive Summary



Executive Summary

Market background

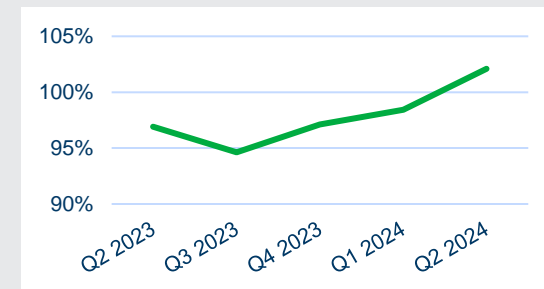
- The second quarter of 2024 saw inflation rates largely soften towards central banks' targets for most developed market economies. This set the stage for a shift towards monetary policy easing.
- Despite this, bond yields rose over the quarter as inflation data came in above market expectations in Q1 and April, especially in the US. Equity markets, barring Japanese equities, continued to rally, with emerging market equities outperforming developed markets.
- Headline inflation in the UK fell to 2.0% in May from 3.2% in March. This was led by a slowdown in the cost of food. However, core inflation remains elevated at 3.5%. The Bank of England maintained interest rates at 5.25%.

Mercer market views

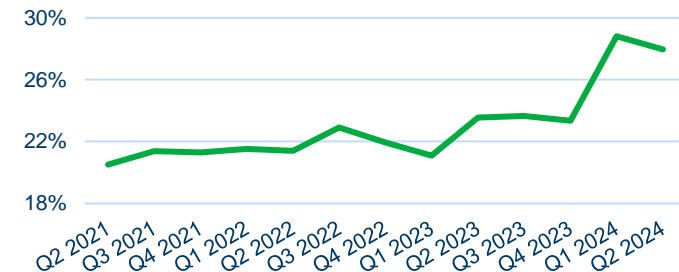
- We believe the US economy is slowing which should lead to further labour market loosening. This should lead to lower inflation allowing the Fed to cut interest rates. We believe this creates an environment where risk assets should perform strongly. We continue to remain wary about equity valuations and corporate earnings forecasts, particularly given higher bond yields. However, we continue to believe further upside is likely and that favourable macroeconomic conditions balances stretched valuations.

Funding level and risk

- The funding level is estimated to have increased over the quarter to c. 102% as the value of the assets fell by less than the estimated present value of the liabilities.
- The funding level is estimated to be c. 5% higher over the year to 30 June 2024 (as illustrated to the right).



- The Value-at-Risk decreased over the quarter to £1,604m, and to 28% as a percentage of liabilities.
- The increase in Q1 2024 was primarily due to the agreed reduction in coverage of the Equity Protection Strategy.



Executive Summary

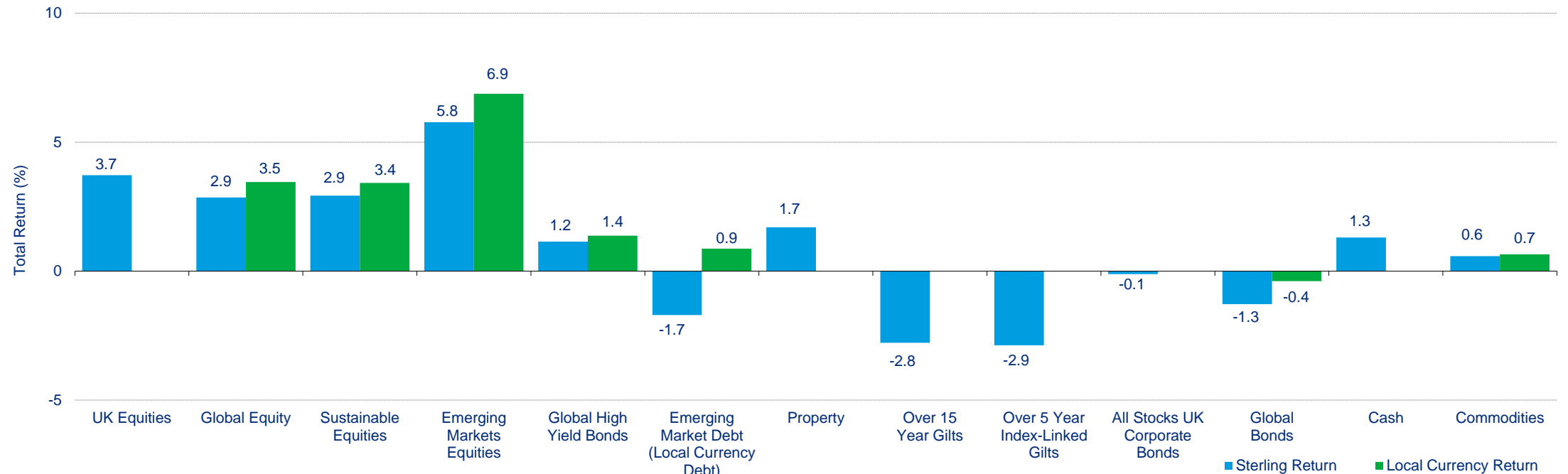
	<ul style="list-style-type: none"> Portfolio absolute returns were mixed. The biggest driver of the overall negative return was the LDI and Corporate Bond portfolios, due to rising interest rates. Equity was the largest contributor to returns, some of which was offset by the Equity Protection strategy. Multi-Asset Credit and the Currency Hedge added to returns, whilst Property detracted. 																	
<p>Performance</p>	<ul style="list-style-type: none"> Underperformance relative to the strategic benchmark over the one year period was mainly due to the active equity funds underperforming, as well as negative returns from the Equity Protection strategy (as underlying equity returns were positive). Elsewhere underlying relative performance was mixed. The main drivers of underperformance over three years were the active equity, Equity Protection, Overseas Property and Secured Income mandates. The Currency Hedge added to returns over the one year period due to the relative strengthening of Sterling, but conversely detracted over three years. Absolute returns compared to the strategic returns modelled at the strategy review in 2023 have been positive for all of the Equity and Liquid Growth assets, except for the Diversified Returns portfolio which is marginally negative They have been negative for the Illiquid Growth assets except for Private Debt cycle 2. However many of these assets are still in the drawdown phase. 	<table border="1"> <thead> <tr> <th></th> <th>3 Months (%)</th> <th>1 Year (%)</th> <th>3 Years (% p.a.)</th> </tr> </thead> <tbody> <tr> <td>Total Fund (1)</td> <td>-0.3</td> <td>7.6</td> <td>1.6</td> </tr> <tr> <td>Strategic Benchmark (2) (ex currency hedge)</td> <td>2.2</td> <td>10.7</td> <td>6.5</td> </tr> <tr> <td>Relative (1 - 2)</td> <td>-2.5</td> <td>-3.1</td> <td>-4.9</td> </tr> </tbody> </table>		3 Months (%)	1 Year (%)	3 Years (% p.a.)	Total Fund (1)	-0.3	7.6	1.6	Strategic Benchmark (2) (ex currency hedge)	2.2	10.7	6.5	Relative (1 - 2)	-2.5	-3.1	-4.9
	3 Months (%)	1 Year (%)	3 Years (% p.a.)															
Total Fund (1)	-0.3	7.6	1.6															
Strategic Benchmark (2) (ex currency hedge)	2.2	10.7	6.5															
Relative (1 - 2)	-2.5	-3.1	-4.9															
<p>Asset allocation and strategy</p>	<ul style="list-style-type: none"> A net amount of c. £42m was drawn down to private market portfolios during the quarter. Amongst this was a large drawdown of c. £36m to Secured Income cycle 3, after which the commitments to this asset class have now been fully drawn down. £50m of collateral was withdrawn from the BlackRock QIAIF during the period. The Fund currently has an overweight to Equity (although the underlying allocations are within their target ranges), in part reflecting relative outperformance to other parts of the portfolio over the past year. 																	
<p>Liability hedging mandate</p>	<ul style="list-style-type: none"> BlackRock was in compliance with the investment guidelines over the quarter. The interest rate and inflation trigger framework was revised and reinstated in October 2023. Following the reinstatement of the framework, several interest rate triggers were hit leading BlackRock to trade up to the target (39% as a % of assets) aggregate interest rate hedge ratio. The inflation hedge ratio was c. 22% as a % of assets at the same date. The trigger framework was subsequently paused whilst a wider review of the Fund's liquidity framework is undertaken. 																	
<p>Collateral position</p>	<ul style="list-style-type: none"> Following the reduction in the equity protection coverage ratio in March, the Fund has adopted an updated collateral monitoring framework reflecting the significant change in exposures within the risk management portfolio. Inclusive of assets within the collateral waterfall and the updated collateral monitoring framework, there was a total interest rate buffer of 6.5% as at 30 June 2024. 																	

Market Background



Market Background

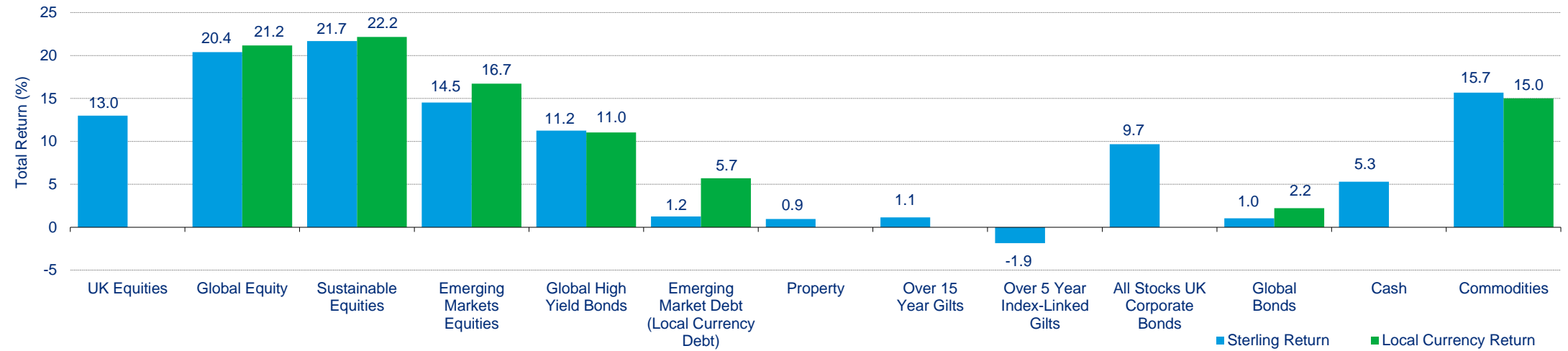
Return over 3 months to 30 June 2024 (%)



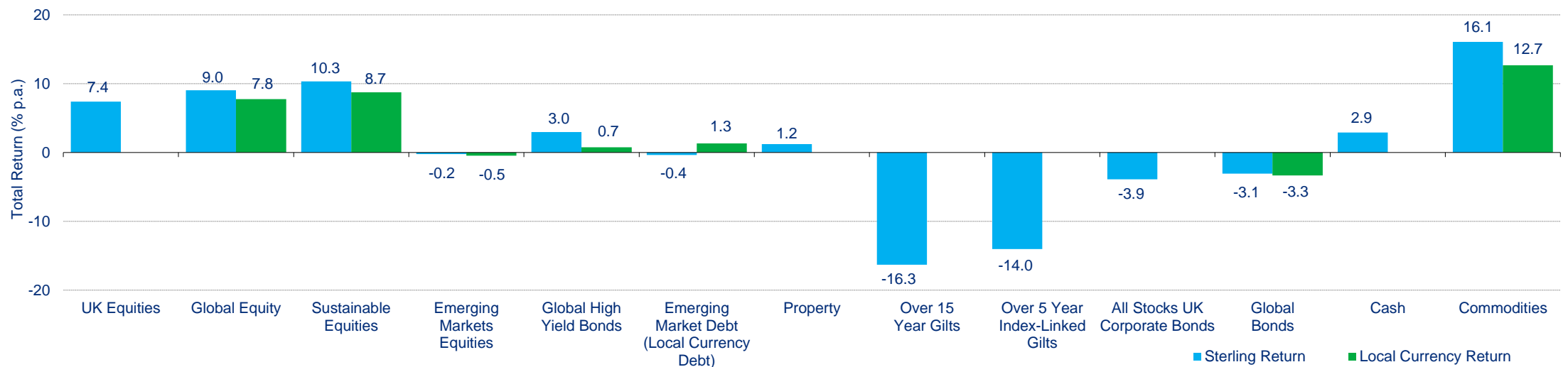
The second quarter of 2024 saw inflation rates largely soften towards central banks' targets for most developed market economies. This set the stage for a shift towards monetary policy easing. The European Central Bank cut interest rates in June. Cooling inflation and a gradual loosening of the labour markets in the US prompted markets to price in two cuts by the US Federal Reserve by the end of 2024. The timing of potential rate cuts by the Bank of England was pushed to August despite waning price pressures, as service inflation remains elevated. Despite this, bond yields rose over the quarter as inflation data came in above market expectations in Q1 and April, especially in the US. Equity markets, barring Japanese equities, continued to rally, with emerging market equities outperforming developed markets. Political volatility remained high with a snap election called in the UK & France while the first TV debate of the US election campaign took place in June.

Market Background – 1 & 3 Years

Return over 12 months to 30 June 2024 (%)



Return over 3 years to 30 June 2024 (% p.a.)



Funding Level and Risk

3

Funding Level and Deficit

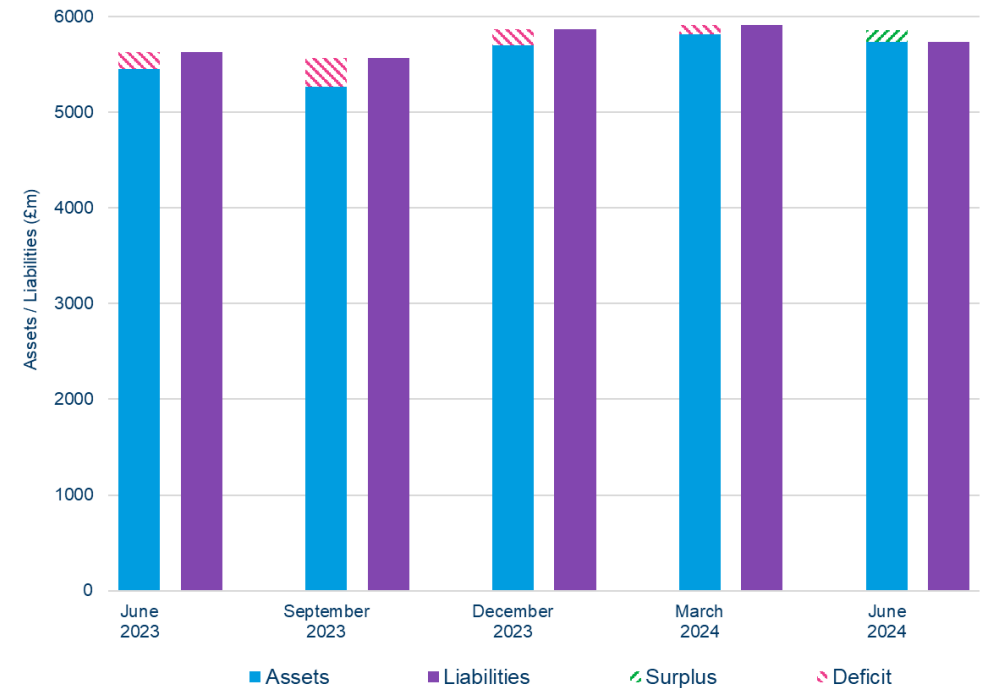
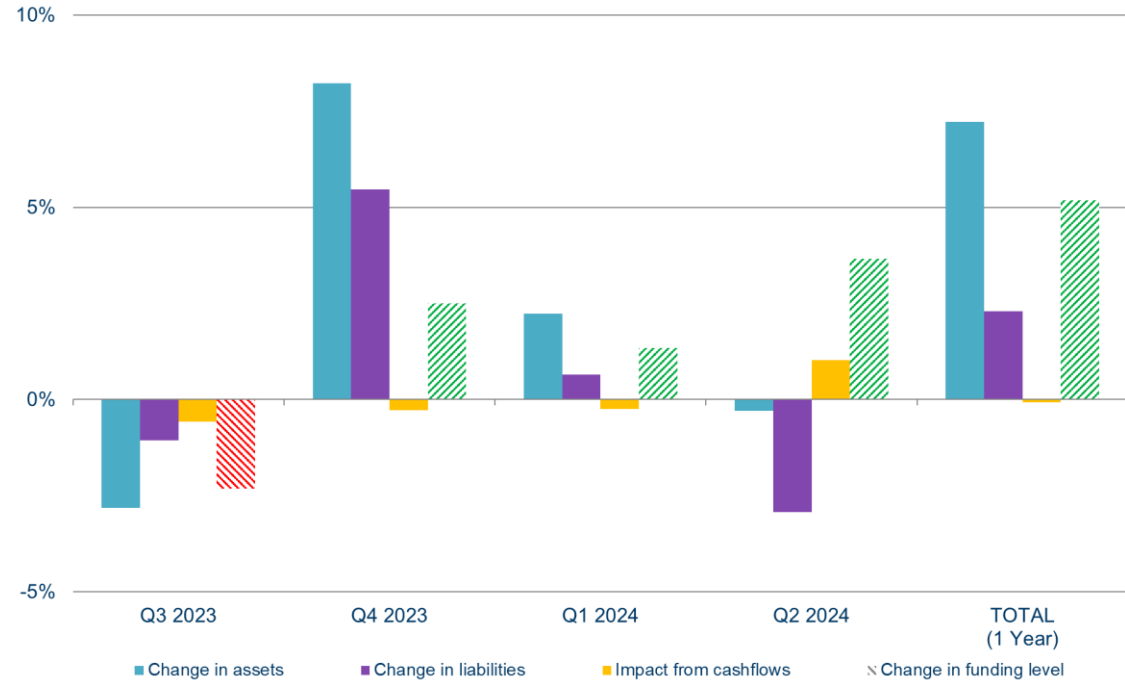
The Fund's assets returned -0.3% over the quarter, whilst the liabilities are estimated to have decreased by c. 2.9%.

The combined effect of this saw the estimated funding level increase to c. 102%.

The funding level is estimated to be c. 5% higher over the year to 30 June 2024.

The rise in the estimated value of the liabilities shown for Q4 2023 includes the impact of a move to a lower actuarial discount rate basis of CPI + 2.5% (from CPI + 2.8%), which is reflected from 31 December 2023 onwards.

A surplus of c. £120m is now estimated, compared to the deficit last quarter of c. £92m.



Liability values are estimated by Mercer. They are based on the actuarial valuation assumptions as at 31 March 2022 and the 'CPI plus' discount basis. Impact figures are estimated by Mercer.

Risk Decomposition – 3 Year Value at Risk

- The two charts below illustrate the main risks that the Fund is exposed to, and the size of these risks in the context of the change in the deficit position.
- The purpose of showing these is to ensure there is an awareness of the risks faced and how they change over time, and to initiate debate on an ongoing basis around how to best manage these risks, so as not to lose sight of the ‘big picture’.
- The final columns show the estimated 95th percentile Value-at-Risk (VaR) over a one-year period. In other words, if we consider a downside scenario which has a 1-in-20 chance of occurring, what would be the impact on the deficit relative to our ‘best estimate’ of what the deficit would be in three years’ time.

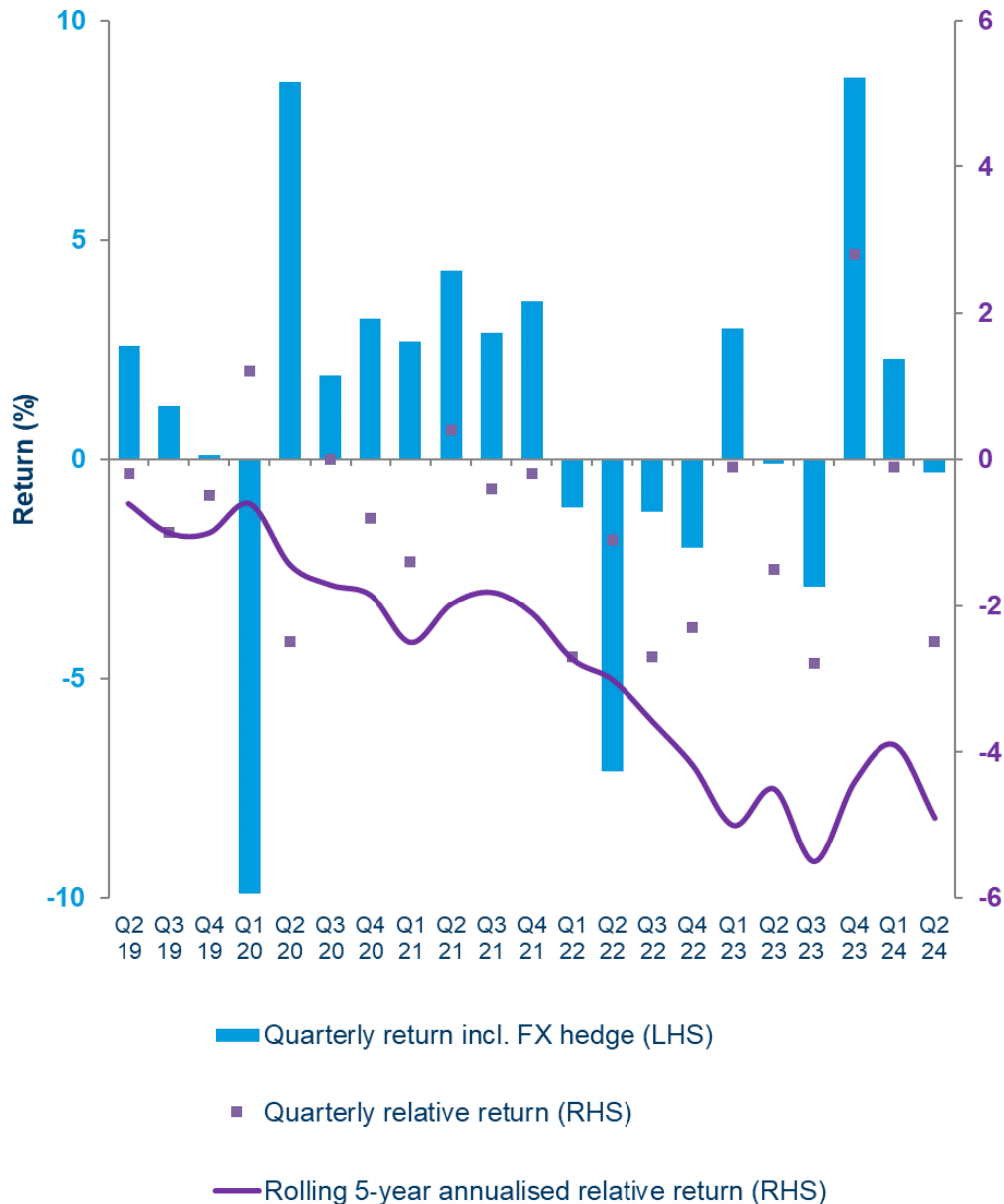


- As at 30 June 2024, if a 1-in-20 ‘downside event’ occurred over the next three years, the funding position could deteriorate by at least an additional **£1.6bn**.
- Each bar to the left of the total represents the contribution to this total risk from the primary underlying risk exposures (interest rates and inflation, changes in credit spreads, volatility of alternative assets and equity markets, and the benefit from equity options).
- Overall **the VaR decreased by £99m over the quarter**. This was due to an overall decrease in underlying volatility assumptions, as well as some modelling refinements.
- As a percentage of liabilities, VaR decreased to from 29% to 28%.

Performance Summary



Total Fund Performance



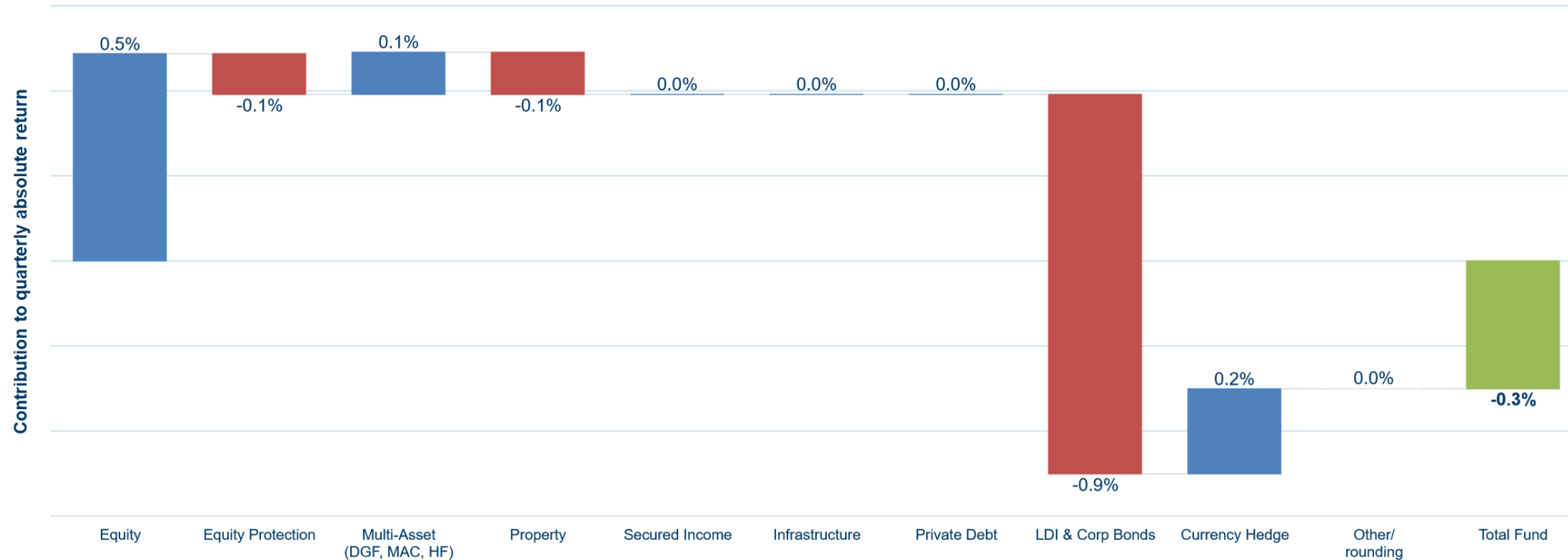
	3 Months (%)	1 Year (%)	3 Years (% p.a.)
Total Fund (1)	-0.3	7.6	1.6
Total Fund (ex currency hedge)	-0.5	7.4	2.0
Strategic Benchmark (2) (ex currency hedge)	2.2	10.7	6.5
Relative (1 - 2)	-2.6	-3.2	-4.8

Source: Custodian, Mercer estimates. Returns are net of fees. 'Relative' figures may not sum due to rounding.

Commentary

- As illustrated on the next slide, the marginal negative return for the Fund over the quarter was driven by the LDI and Corporate Bonds portfolio due to its interest rate exposure. Equity was the largest contributor to returns, some of which was offset by the Equity Protection strategy. Multi-Asset Credit and the Currency Hedge added to returns, whilst Property detracted.
- Relative performance was negative for all active mandates except for some of the Secured Income and Infrastructure mandates.
- Underperformance relative to the strategic benchmark over the one year period was mainly due to the active equity funds underperforming, as well as negative returns from the Equity Protection strategy (as underlying equity returns were positive).
- Elsewhere underlying relative performance was mixed.
- The main drivers of underperformance over three years were the active equity, Equity Protection, Overseas Property and Secured Income mandates.
- The Currency Hedge added to returns over the one year period due to the relative strengthening of Sterling, but conversely detracted over three years.

Total Fund Performance Attribution – Quarter



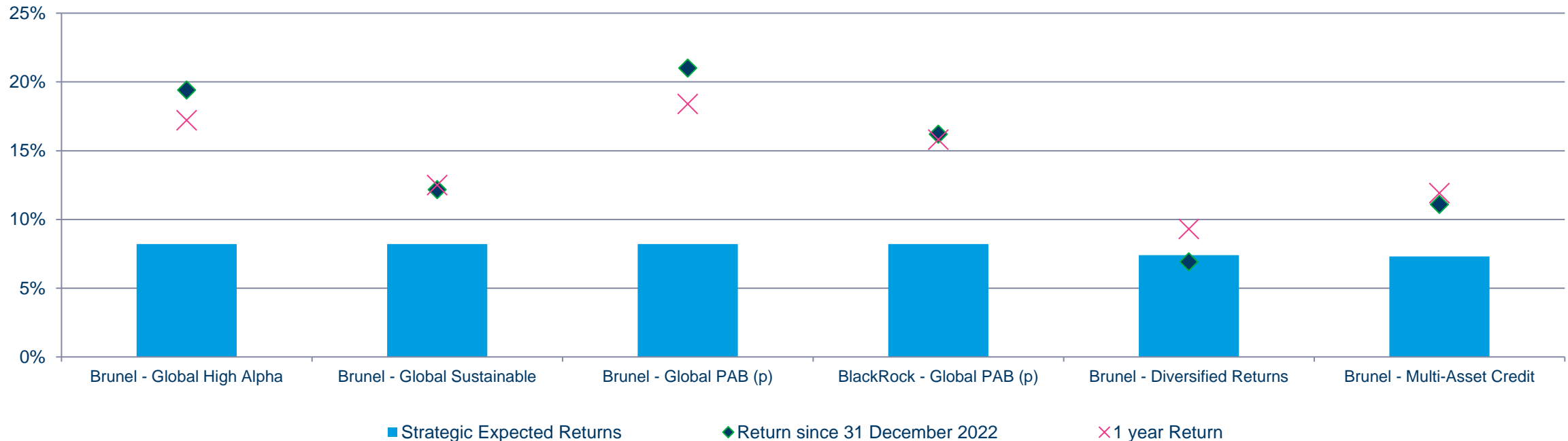
Source: Custodian and Mercer estimates

'Other' contributions to the total can include the relatively small holdings in the ETF, cash, the impact of cashflows and terminated mandates, as well as rounding.

The marginal negative return on Fund assets over the quarter was driven by the LDI and Corporate Bonds portfolio due to its interest rate exposure. Equity was the largest contributor to returns, some of which was offset by the Equity Protection strategy. Multi-Asset Credit and the Currency Hedge added to returns, whilst Property detracted.

Performance vs. Expected Strategic Returns

Growth Asset	Brunel Global High Alpha	Brunel Global Sustainable	Brunel / BlackRock Passive Global PAB	Brunel Diversified Returns	Brunel Multi-Asset Credit
Benchmark Allocation	10.5%	10.5%	20.5%	6.0%	6.0%
Commentary	Returns above expectations since December 2022 due to equity market strength, though mandate has underperformed the benchmark.	Returns above expectations since December 2022 due to equity market strength, though mandate has underperformed the benchmark.	Brunel PAB (FTSE index) returns above expectations since December 2022 due to equity market strength. BlackRock synthetic PAB (MSCI index) returns above expectations since May 2023; when exposure was put in place.	Returns marginally below expectations since December 2022, despite strong absolute returns over most of the past year.	Returns above expectations since December 2022 thanks to strength in high-yield debt markets.

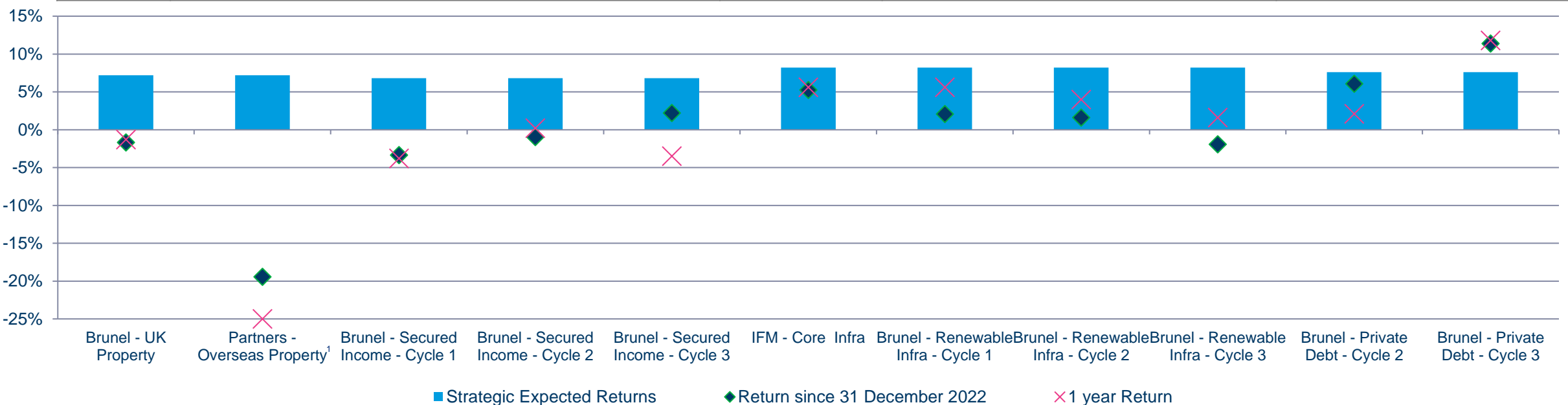


Notes:

We have illustrated the performance of the key mandates within the Fund's investment strategy. Actual returns are from 31 December 2022 to 30 June 2024, except if otherwise stated below. Returns for periods over a year have been annualised. The strategic expected returns are from the 2023 strategy review, which reflect the 10 year mean Mercer Q4 2022 asset model assumptions.

Performance vs. Expected Strategic Returns

Growth Asset	Brunel UK Property	Partners Overseas Property	Brunel Secured Income	IFM Core Infra	Brunel Renewable Infra	Brunel Private Debt
Benchmark allocation	3.5%	3.5%	9.0%	4.0%	5.0%	4.5%
Commentary	Returns below expectations since December 2022 due to the challenges seen in Property markets. Time horizon for Secured Income Cycle 3 is since June 2023; when it first drew down capital.			Returns slightly below expectations since December 2022. Returns prior to this date, since the mandate's inception, are noticeably stronger.	Returns for all cycles below expectations since December 2022. Mandates are still in the drawdown phase; the first drawdowns were in January 2019, October 2020 and October 2022 respectively. Returns for cycles 1 and 2 are stronger over their since inception periods.	Returns below with expectations for cycle 2 but above expectations for cycle 3, since December 2022. Mandates are still in the drawdown phase; the first drawdowns were in September 2021 and December 2022 respectively.



Notes:

We have illustrated the performance of the key mandates within the Fund's investment strategy. Actual returns are from 31 December 2022 to 30 June 2024, except if otherwise stated below. Returns for periods over a year have been annualised. The strategic expected returns are from the 2023 strategy review, which reflect the 10 year mean Mercer Q4 2022 asset model assumptions.

¹ Returns are shown up to 31 March 2024, as this is the latest data available.

Mandate Performance to 30 June 2024

Manager / Asset Class	3 Months			1 Year			3 Year			3 Year Performance Target (% p.a.)**	3 Year Performance vs Target
	Fund (%)	B'mark (%)	Relative (%)	Fund (%)	B'mark (%)	Relative (%)	Fund (% p.a.)	B'mark (% p.a.)	Relative (% p.a.)		
Brunel Global High Alpha Equity	1.1	2.7	-1.6	17.2	21.4	-4.2	6.8	10.6	-3.8	+2-3	Target not met
Brunel Global Sustainable Equity	-0.5	2.9	-3.4	12.5	20.6	-8.1	3.5	9.1	-5.6	+2	Target not met
Brunel Passive Global Equity Paris-Aligned	2.8	2.8	0.0	18.4	18.4	0.0	N/A	N/A	N/A	-	N/A (p)
MSCI World Paris-Aligned (Synthetic)	1.7	1.7	0.0	15.8	15.8	N/A	N/A	N/A	N/A	-	N/A (p)
Brunel Diversified Returns Fund	-0.5	2.0	-2.5	9.3	8.4	+0.9	2.8	6.0	-3.2	-	Target not met
Brunel Multi-Asset Credit	1.9	2.3	-0.4	11.9	9.4	+2.5	2.7	7.0	N/A	-	N/A
Brunel UK Property	0.6	1.4	-0.8	-1.3	0.0	-1.3	0.4	0.0	+0.4	-	Target met
Partners Overseas Property*	-4.3	2.5	-6.8	-25.0	10.0	-35.0	-8.1	10.0	-18.1	-	Target not met
Brunel Secured Income - Cycle 1	-0.7	0.8	-1.5	-3.8	2.0	-5.8	-2.6	6.4	-9.0	+2	Target not met
Brunel Secured Income - Cycle 2	1.6	0.8	+0.8	0.2	2.0	-1.8	0.9	6.4	-5.5	+2	Target not met
Brunel Secured Income - Cycle 3	0.2	0.8	-0.6	-3.5	2.0	-5.5	N/A	N/A	N/A	+2	N/A
IFM Core Infrastructure	0.7	2.5	-1.8	5.6	10.5	-4.9	8.2	8.1	+0.1	-	Target met
Brunel Renewable Infrastructure - Cycle 1	0.2	0.8	-0.6	5.6	2.0	+3.6	8.2	6.4	+1.8	+4	Target not met
Brunel Renewable Infrastructure - Cycle 2	1.2	0.8	+0.4	4.0	2.0	+2.0	10.3	6.4	+3.9	+4	Target not met
Brunel Renewable Infrastructure - Cycle 3	3.2	0.8	+2.4	1.6	2.0	-0.4	N/A	N/A	N/A	+4	N/A
Brunel Private Debt - Cycle 2	-0.3	2.3	-2.6	2.1	9.4	-7.3	N/A	N/A	N/A	-	N/A
Brunel Private Debt - Cycle 3	0.9	2.3	-1.4	11.8	9.4	+2.4	N/A	N/A	N/A	-	N/A
BlackRock Corporate Bonds	-0.8	-0.8	0.0	10.2	10.2	0.0	-9.1	-9.1	0.0	-	N/A (p)
BlackRock LDI	-4.0	-3.5	-0.5	-1.2	-1.8	+0.6	-3.5	-3.0	-0.5	-	N/A (p)
Equity Protection Strategy	-0.4	N/A	N/A	-2.5	N/A	N/A	-2.3	N/A	N/A	-	N/A

Source: Investment Managers, Custodian, Mercer estimates. Returns are net of fees, unless otherwise stated. Returns are in GBP terms

From this report onwards, relative returns are calculated arithmetically.

A summary of the benchmarks for each of the mandates is given in the Appendix.

Green = mandate exceeded target. Red = mandate underperformed target. Black = mandate performed in line with target (mainly reflecting passive mandates).

Performance for Partners in IRR terms. Performance for IFM is in TWR terms.

Performance of the Equity Protection Strategy is estimated by Mercer based on the change in market value of the options over time, accounting for realised profit/loss upon rolling of the strategy.

Performance for the LDI portfolio is estimated by Mercer based on the change in exposure. These returns are gross of fees.

Performance for MSCI World Paris-Aligned (Synthetic) has been converted to GBP by Mercer, as the associated index is denominated in USD.

*Partners performance is to 31 March 2024, as this is the latest data available.

**Where the outperformance target has not already been incorporated into the benchmark returns shown. See Appendix for further details.

Asset Allocation



Valuation by Asset Class

Asset Class	Start of Quarter (£'000)	End of Quarter (£'000)	Start of Quarter (%)	End of Quarter (%)	Benchmark (%)	Ranges (%)	Relative (%)
Global Equity	755,210	772,755	13.0	13.2	10.5	5.5 - 15.5	+2.7
Global Sustainable Equity	666,871	663,348	11.5	11.3	10.5	5.5 - 15.5	+0.8
Paris-Aligned Equity*	1,517,779	1,561,760	26.1	26.7	20.5	12.5 - 28.5	+6.2
Diversified Returns Fund	373,170	371,464	6.4	6.3	6.0	3 - 9	+0.3
Fund of Hedge Funds**	23,907	17,914	0.4	0.3	-	No set range	+0.3
Multi-Asset Credit	340,487	347,111	5.9	5.9	6.0	3 - 9	-0.1
Property	299,369	294,347	5.1	5.0	7.0	No set range	-2.0
Secured Income	600,319	629,318	10.3	10.7	9.0	No set range	+1.7
Core Infrastructure	228,645	230,142	3.9	3.9	4.0	No set range	-0.1
Renewable Infrastructure	206,889	216,134	3.6	3.7	5.0	No set range	-1.3
Private Debt	203,367	209,166	3.5	3.6	4.5	No set range	-0.9
Local / Social Impact	35,085	34,984	0.6	0.6	3.0	No set range	-2.4
Corporate Bonds	181,886	180,396	3.1	3.1	2.0	No set range	+1.1
LDI & Equity Protection	1,340,450	1,244,564	23.0	21.2	12.0	No set range	+9.2
Synthetic Equity Offset*	-1,090,079	-1,122,022	-18.7	-19.2	-	-	-
Other***	134,623	206,299	2.3	3.5	-	0 - 5	+3.5%
Total	5,818,000	5,857,702	100.0	100.0	100.0		

Source: Custodian, Investment Managers, Mercer. Red numbers indicate the allocation is outside of tolerance ranges.

Totals may not sum due to rounding.

*Paris-Aligned includes synthetic exposure via the BlackRock QIF; Synthetic Equity Offset reflects an offsetting value to account for the difference between the exposure to equity markets and the actual mark to market value of the holding.

**Mandate due to be terminated.

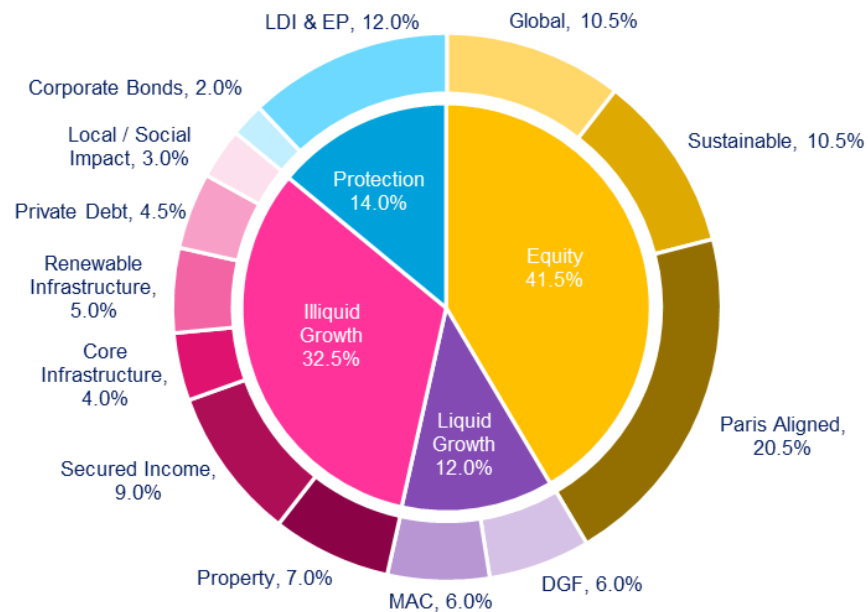
***Valuation includes internal cash, the ETF and currency instruments.

Valuation by Manager

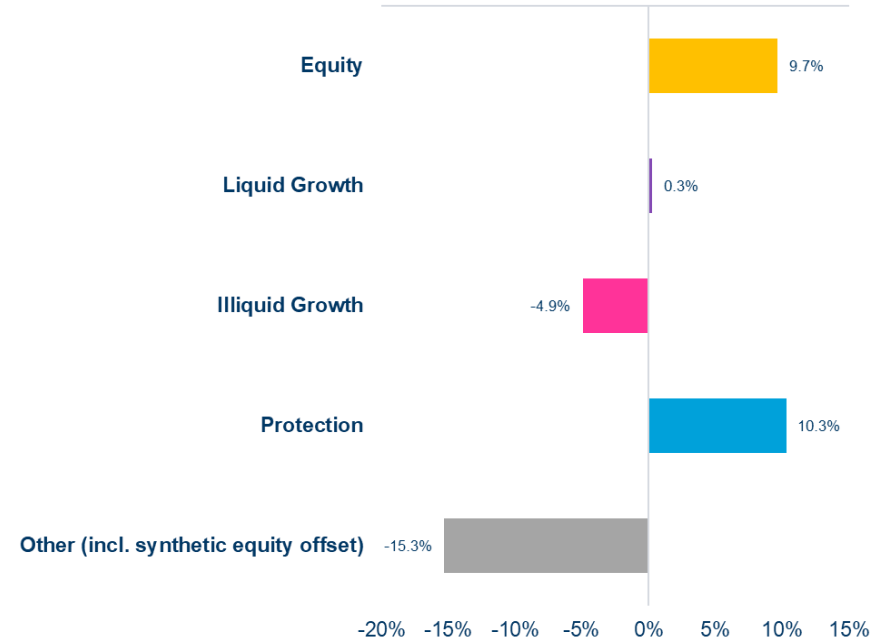
Manager	Asset Class	Start of Quarter (£'000)	Cashflows (£'000)	End of Quarter (£'000)	Start of Quarter (%)	End of Quarter (%)
Brunel	Global High Alpha Equity	720,796	-	728,542	12.4	12.4
Brunel	Global Sustainable Equity	666,871	-	663,348	11.5	11.3
Brunel	Passive Global Equity Paris Aligned	427,700	-11	439,738	7.4	7.5
BlackRock	MSCI Paris-Aligned (Synthetic)*	1,090,079	-	1,122,022	18.7	19.2
Brunel	Diversified Returns Fund	373,170	-	371,464	6.4	6.3
JP Morgan	Fund of Hedge Funds	23,907	-6,425	17,914	0.4	0.3
Brunel	Multi-Asset Credit	340,487	-	347,111	5.9	5.9
Brunel	UK Property	178,154	-131	179,251	3.1	3.1
Schroders	UK Property	13,185	-31	13,967	0.2	0.2
Partners	Overseas Property	108,030	-	101,130	1.9	1.7
Brunel	Secured Income – Cycle 1	296,092	-1,961	292,196	5.1	5.0
Brunel	Secured Income – Cycle 2	101,660	-3,179	100,108	1.7	1.7
Brunel	Secured Income – Cycle 3	202,568	34,049	237,013	3.5	4.0
IFM	Core Infrastructure	228,645	-	230,142	3.9	3.9
Brunel	Renewable Infrastructure – Cycle 1	112,995	270	113,570	1.9	1.9
Brunel	Renewable Infrastructure – Cycle 2	79,509	5,161	85,733	1.4	1.5
Brunel	Renewable Infrastructure – Cycle 3	14,385	1,853	16,831	0.2	0.3
Brunel	Private Debt – Cycle 2	161,102	-	160,676	2.8	2.7
Brunel	Private Debt – Cycle 3	42,265	5,770	48,490	0.7	0.8
BlackRock	Corporate Bonds	181,886	-	180,396	3.1	3.1
BlackRock	LDI & Equity Protection	1,340,450	-50,000	1,244,564	23.0	21.2
BlackRock	<i>Synthetic Equity Offset*</i>	-1,090,079	-	-1,122,022	-18.7	-19.2
Record	Currency Hedging (incl. collateral)	46,603	-	55,727	0.8	1.0
BlackRock	ETF	3,354	-	3,400	0.1	0.1
Schroders Greencoat	Wessex Gardens	35,085	-	34,984	0.6	0.6
-	Internal Cash	118,635	71,492	190,949	2.0	3.3
-	Residual Assets	446	-	435	0.0	0.0
Total		5,818,000	56,843	5,857,702	100.0	100.0

Positioning relative to target

Strategic Asset Allocation (“SAA”)



Relative positioning



Commentary

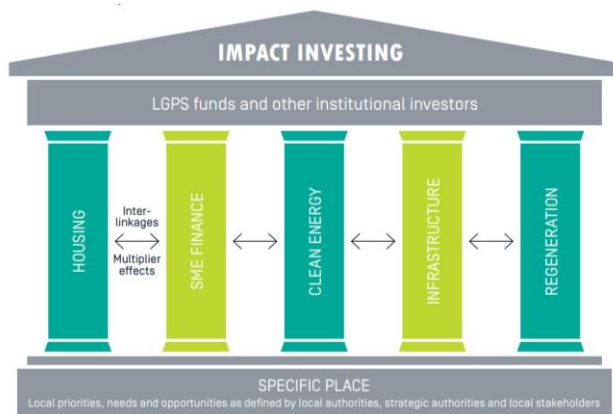
- The Plan last updated its Strategic Asset Allocation as part of the 2023 Investment Strategy Review.
- The right hand side chart displays the actual relative weights of the key portfolio building blocks compared to the SAA:
 - The overweight to Equity reflects relative outperformance to other parts of the portfolio over the past year.
 - The underweight to Illiquid Growth reflects recent relative underperformance, and the fact that in aggregate, capital is still being drawn (i.e. in excess of distributions being returned).
 - The overweight to Protection reflects the collateral boost provided by the synthesising of some of the Equity allocation; meaning that in practice an overweight to this building block is likely to persist and is unlikely to trigger any consideration for action, which would continue to be driven more specifically by collateral adequacy requirements.
- A net amount of c. £42m was drawn down to private market portfolios during the quarter. Amongst this was a large drawdown of c. £36m to Secured Income cycle 3, after which the commitments to this asset class have now been fully drawn down.
- £50m of collateral was withdrawn from the BlackRock QIAIF during the period.

Current Topics

6

Current Topics

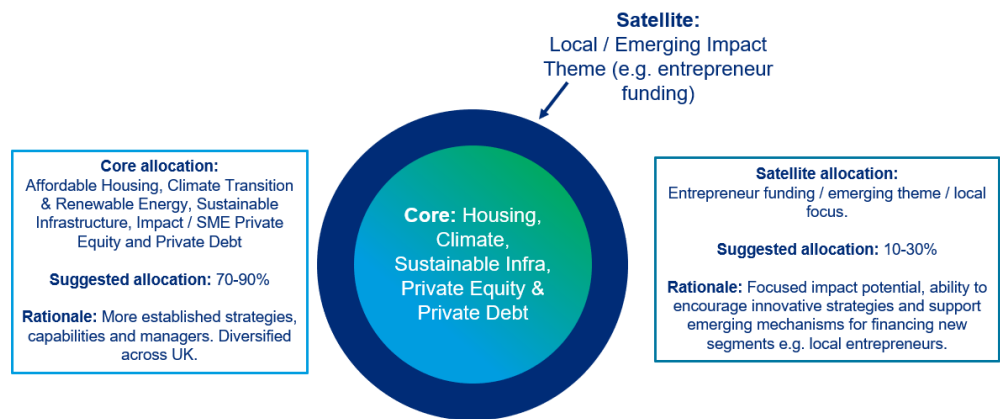
Investing in the UK with Impact



Place-based impact investing considerations:

1. Impact intentionality
2. Define place
3. Community / stakeholder engagement
4. Impact measurement
5. Collaboration

Building a UK Impact portfolio – Example approach

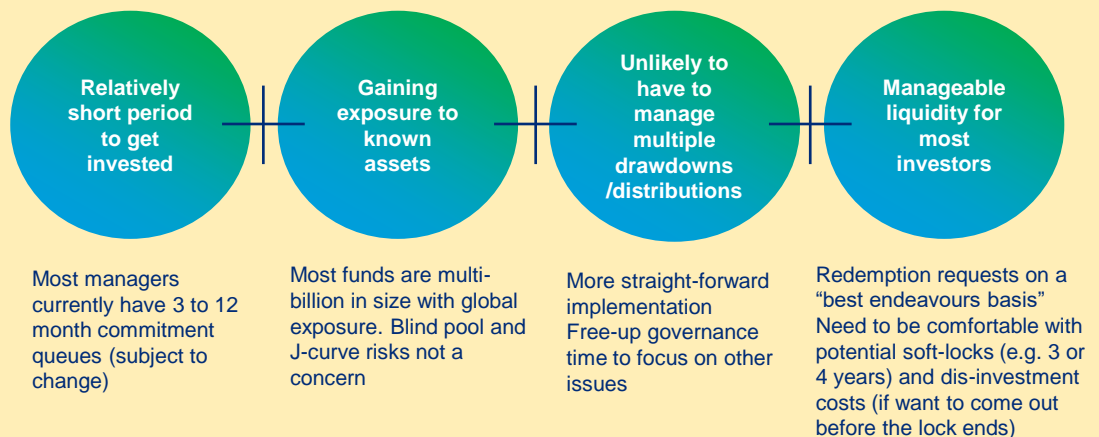


Relevance to the Fund

✓
The Fund already has a strategic allocation to an Impact Portfolio, for which the composition looks broadly similar to the illustrated example.
It has already committed to 'Core' investments in Housing and Climate, and the current priority is finding investible opportunities related to the supporting of local small and medium sized enterprises, which fits into the 'Satellite' allocation of this example.

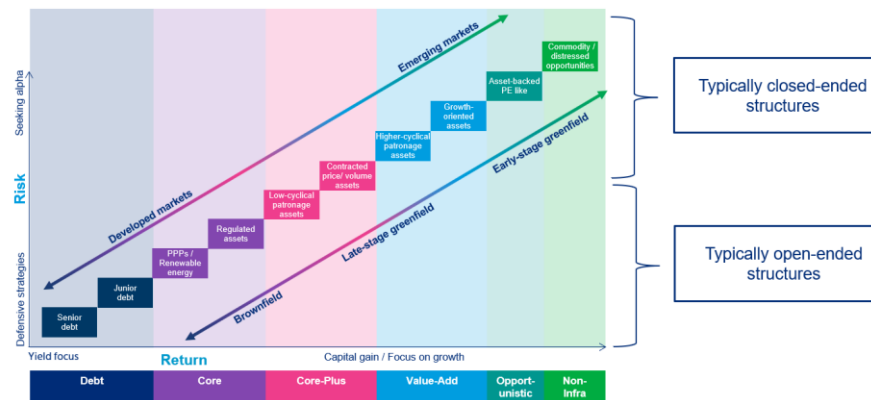
Open-Ended Infrastructure (Unlisted Equity)

Why consider Open Ended implementation?



Less complexity than traditional closed ended investment route

A varied risk and return spectrum:



For illustration and educational purposes only. These are the views of Mercer at this time and are subject to change and are not guaranteed.

Relevance to the Fund

✓
The Fund has exposure to open-ended infrastructure through the IFM Global Infrastructure Fund. Its place within the portfolio has been reaffirmed relatively recently, and the key benefits of this assets are echoed here.

Current Topics

Opportunities on the Secondary Market

Background

- Typically closed-ended funds
- Varying degrees of time left to run-off – some relatively short (sub 5 years)
- Mercer receive indicative pricing (discounts) from brokers for a range of private market assets
- Taking the example of infrastructure equity, initial quoted discounts range from 5% to 25% on but might be higher once negotiated

With some UK DB private sector pension funds looking to sell illiquid private market funds, we are seeing highly rated funds offered at attractive discounts on the secondary market.

Key Considerations

1 – Price Discovery

- Typical to engage a broker to review the market.
- Buyers may need to take the whole of the seller's fund allocation or in some cases the seller will agree to a partial sale.

2 – Acting Swiftly

- Sellers will expect buyers to conduct their due diligence quickly and be able to agree legal agreements to transition ownership (e.g. 1-3 months).
- Liaison and work required relating to the communications between, the buyer and the potential seller, General Partners and broker.

3 – Transfer of Ownership

- Lawyers will be required to agree a transfer agreement and purchase and sale agreement and review underlying fund documentation.

4 – Due Diligence

- Review data on the underlying funds and select appropriate funds to bid on.
- Due diligence undertaken by reviewing information provided by the seller in a data room.
- Manager research may be helpful but there could also be limitations (e.g. if research is old).

Key Risks

- Bids from potential buyers may not be accepted
- There could be inherent non-performing assets in the portfolio that need to be worked out. Identifying any realised / unrealised losses is key to the due diligence process.
- Private market funds may struggle to sell on the underlying assets and not achieve the price that is reflected in the net asset value.
- Investors may not get back the full value invested and Internal Rates of Return could be lower than expected.
- A fund's life could be extended.

Mercer's Secondary Activity

Robust deal flow and access to all secondary types, including LP-leds, GP-leds, and other deal types:



Since end of 2020, Mercer deployed nearly \$2bn in >100 secondary transactions across deal types and asset classes (key focus on private equity and infrastructure) and belongs to a small group of regular secondary buyers in the market

¹ As of June 30, 2023; includes 971 managers with active private equity primary, secondary and co-investments across advisory, partial discretion and full discretion clients' portfolios that Mercer monitors and reports on as well as c. 50 brokers we regularly interact with to source secondary transactions.

Relevance to the Fund

The Fund has an established plan for funding its private market strategic allocations in the medium term, so is unlikely to pursue these opportunities directly. Impact Portfolio themes are likely to be too niche / novel to have a noticeable presence on the secondary market. There is exposure to secondaries within the Brunel private market portfolios, which means the Fund does indirectly access the associated benefits.

Appendix

Q2 2024 Equity Market Review

Q2 2024 has been another positive quarter for equity markets. Equity markets, especially in the developed market, are continuing to be narrowly led; with a small number of stocks driving the returns. Corporate earnings have remained resilient while subsiding inflationary pressures has created a more positive macroeconomic environment for equities.

Global equities returned 2.9% in sterling terms and 3.5% in local currency terms while sterling ended broadly flat against the US dollar.

US equities returned 4.1% in local currency terms, whilst European (ex-UK) equities returns 0.8%, and Japanese equities returned 1.4%.

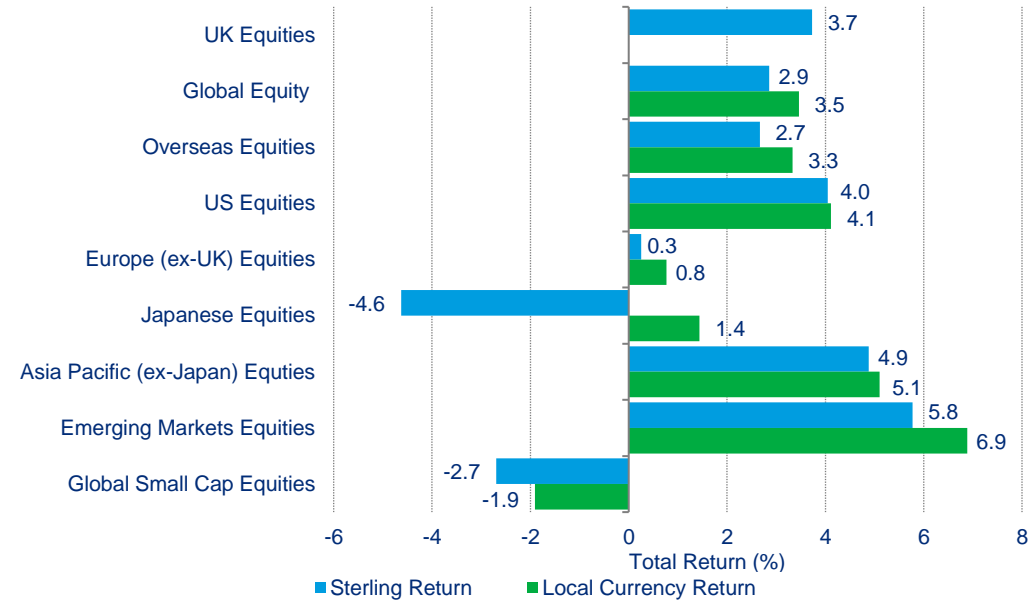
Emerging markets equities returned 6.9% in local terms.

Global small cap stocks returned 1.9% in local terms. Small-cap stocks suffered from confirmation of the higher-for-longer interest rate environment.

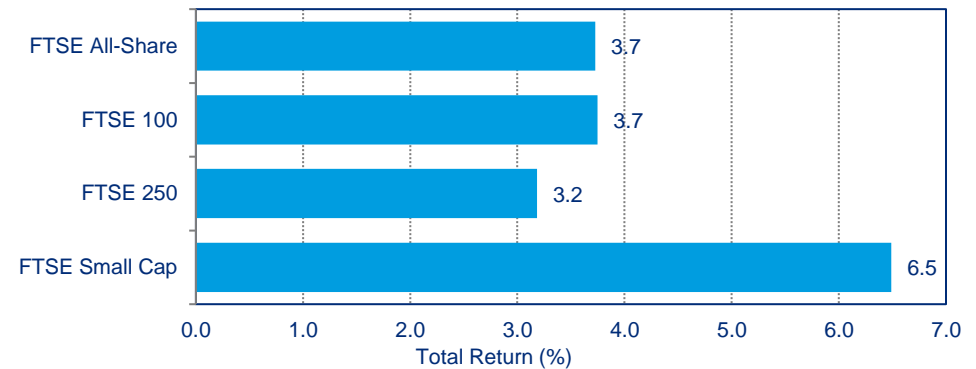
The **FTSE All Share** index returned 3.7% over the quarter, with the large-cap **FTSE 100** index also returning 3.7%. More domestically focused equities (**FTSE 250**) produced positive returns too. The **small-cap** index produced a positive 6.5% return.

Strong performance in telecom and financials supported the UK performance relative to global equities.

Equity Performance



FTSE Performance by Market Cap



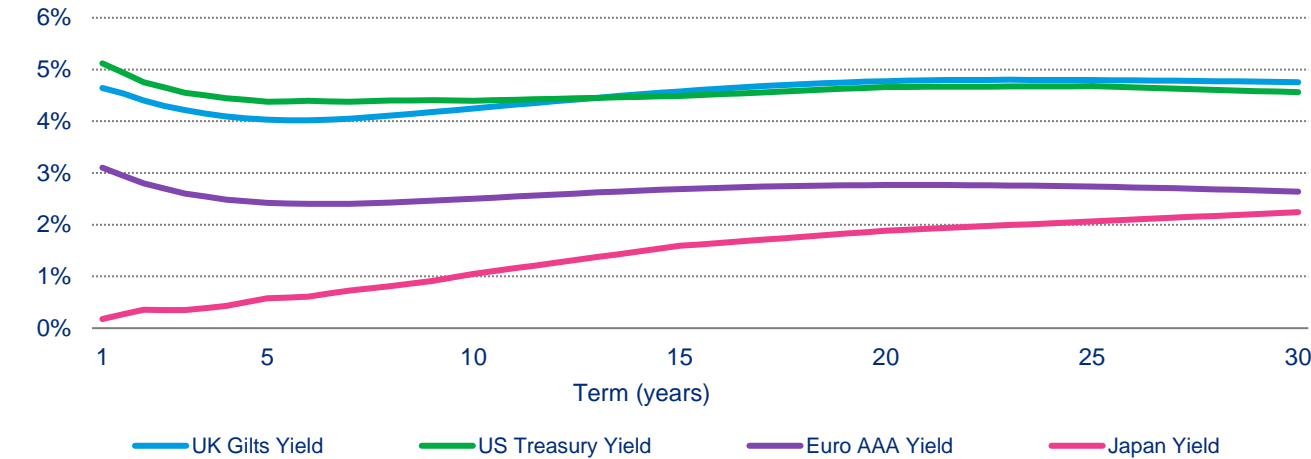
Q2 2024 Bond Market Review

Government Bond Yields

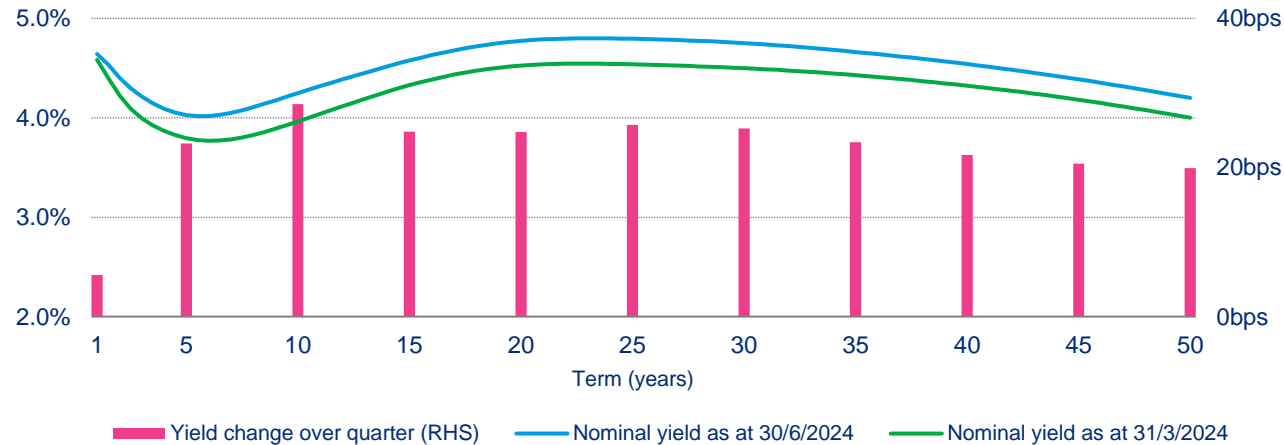
Global government bond yields on the 10-year tenor rose over the quarter (bond yields and prices move in opposite directions). The sell-off in bonds can be attributed to prospects of delayed rate cuts.

In the US, softening inflation and growth, led to bond markets to price in two rate cuts in 2024. In Europe, although the ECB cut interest rates, the subsequent press conference lacked concrete forward guidance, leading markets to perceive the move as hawkish. Meanwhile, easing UK Inflation has set the stage for a BoE rate cut in August.

The 10-year benchmark bond yield in the US, UK, and Germany rose 0.20%, 0.24%, and 0.20%, respectively. Meanwhile, the yield curve across these regions continued to be inverted. 10-year bond yields in Japan also moved past 1.0% on increasing expectations of further policy tightening by the BoJ.

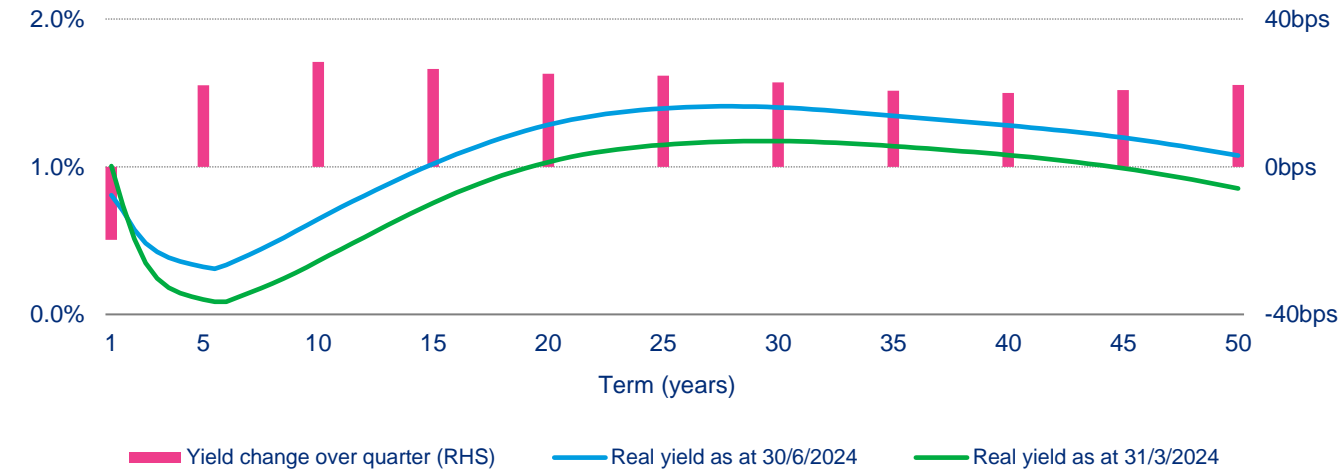


Source: Mercer and Bloomberg

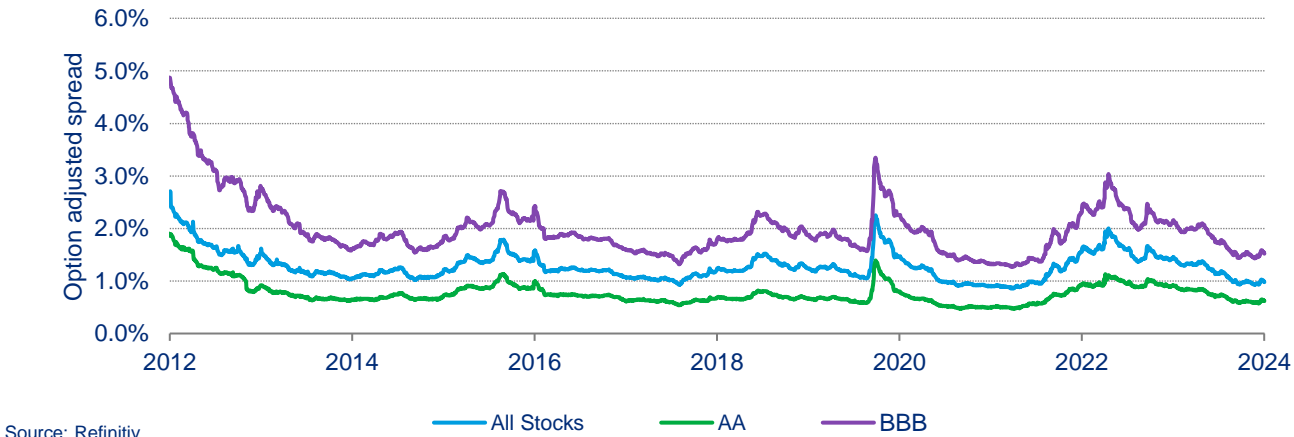


Source: Mercer

Q2 2024 Bond Market Review



Source: Mercer



Source: Refinitiv

UK Index-Linked Gilt Yields

UK real yields rose across most of the curve over the last quarter, with the 10-year tenor increasing 0.28%. There remain concerns that stubborn services inflation and still-healthy wage growth may keep core inflation elevated. UK 10-year breakeven rates finished the quarter at ~3.59% (0.06% lower over the quarter). Despite this, the BoE is widely expected to commence with a rate cut in August.

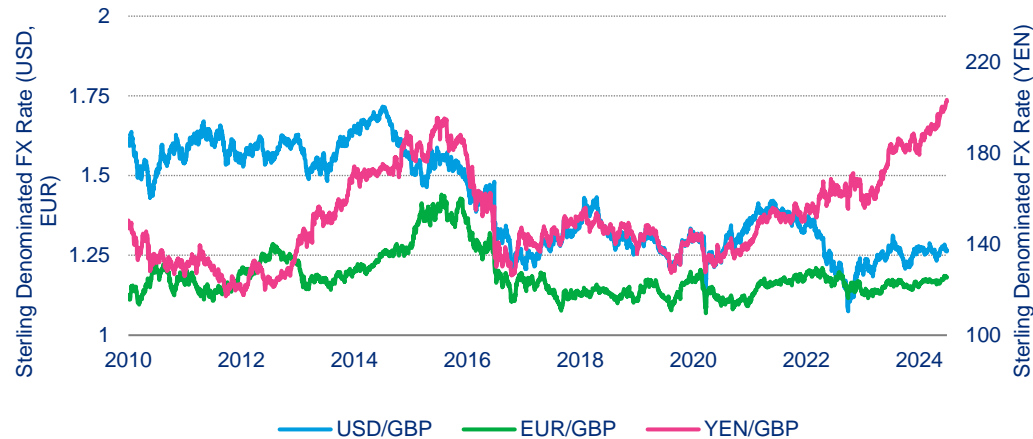
Corporate bonds

Spreads on UK investment-grade credit widened marginally over the quarter, with spreads on lower-rated credit widening more (0.04%) than for higher-rated credit (0.02%).

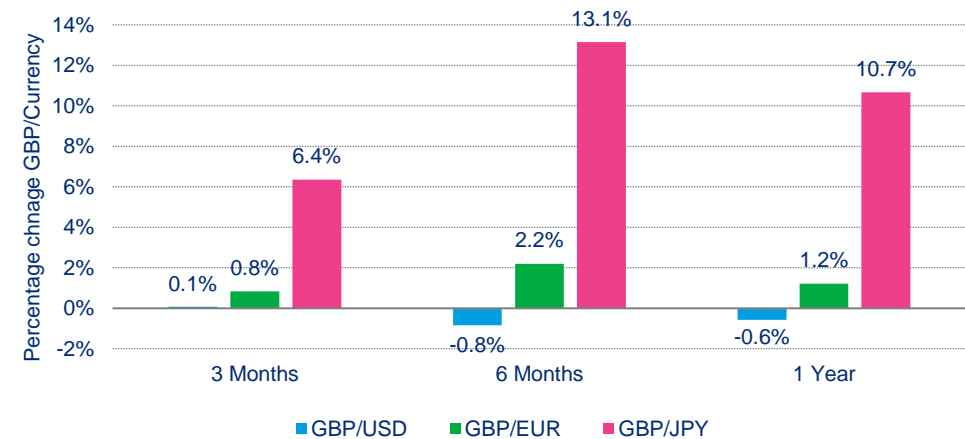
Q2 2024 Currency Market Review

Sterling was broadly unchanged versus US dollar over the quarter, while it appreciated 0.8% and 6.4% against the euro and the yen, respectively. The US dollar index rose a little over 1.0% in the quarter, supported by incoming macro data. On a 12-month basis, sterling significantly outperformed against the yen and marginally versus the euro, while weakening 0.6% against the US dollar.

Sterling Denominated FX Rate



Change in sterling against foreign currencies



Q2 2024 Property

UK property as measured by the MSCI Index increased by 1.7% over the second quarter of 2024.

Dynamic Asset Allocation (DAA)

Dashboard, Positioning & Outlook for UK constrained Portfolio

UK Economic Outlook

UK equities had a strong quarter as the FTSE 100 outperformed global equities (in GBP terms). Global markets were buoyed by the continued moderation in inflation, a resilient economy and positive momentum in corporate earnings. Growth outperformed value by a wide margin while small caps underperformed. Despite falling into a technical recession at the end of last year, the UK economy rebounded strongly in the first quarter of 2024 with real GDP rising 0.7% quarter-on-quarter.¹ This was driven by growth in real disposable income for households as headline inflation hit the central bank's 2% target. That being said, April GDP numbers were a little more disappointing as growth was unchanged on a month-on-month basis.

¹ Office of National Statistics, quarter on quarter growth

Dynamic Asset Allocation (DAA) Positioning

Equities

In terms of UK equities, valuations are attractive, however, we believe they are attractive for a good reason and given mixed outlook for the UK economy we prefer to take risk elsewhere in the equity universe. We remain overweight Emerging Market (EM) equities versus developed market (DM) equities. Economic growth has proven to be more resilient in EM. Policy stimulus in China coupled with ex-China EM central banks easing policy should bolster real household income and boost consumption growth, in turn supporting corporate earnings growth. We expect EM earnings to outpace developed market counterparts over the coming years. We are neutral on small cap equities. With lower pricing power and a lower portion of profitable corporates, small cap equities are more susceptible to a higher-for-longer case, thereby seeing steeper negative earnings revisions. As such, we view the pessimistic sentiment and cheap valuations in small cap equities as justified.

Growth Fixed Income

We retain a favorable view on Emerging Market Debt (EMD) Local Currency (LC) from a tactical perspective. We view it as attractive, expecting yields to decline further as central banks continue a gentle rate cutting cycle. Furthermore, we expect EM currencies to strengthen as central banks cut rate to support growth with inflation back towards target. We are underweight Global High Yield to fund other positions within growth fixed income. Delinquencies from consumer and corporate bankruptcies have been picking up, although from very low levels. As monetary policy conditions remain tight in the developed world it could weigh on corporate balance sheets, especially for companies that are highly levered.

Defensive Fixed Income

From a positioning standpoint, we retain our overweight position in UK gilts. Valuations remain attractive as Gilts sold off more than other developed market government bonds. Bond prices should rise as the Bank of England embarks on an easing cycle while growth remains weak and core inflation falls further towards target. We retain our underweight real gilts vs nominal gilts, expecting the so-called break-even inflation rates to narrow further as inflation rates come down.

Constrained

		Change*
Equities	3%	↑ 2%
DM ex-UK	0%	↑ 2%
UK	0%	
EM	3%	
Small Cap	0%	

Growth Fixed	0%	
EM Debt (HC)	0%	
EM Debt (LC)	2%	
Global HY	-2%	

Defensive Fixed	-3%	↓ 2%
Nominal Gov ex-UK	-3%	↓ 2%
UK Gilts	2%	
Real Gov ex-UK	0%	
UK Index-Linked Gilts	-2%	
IG Credit ex-UK	0%	
UK IG Credit	0%	

Source: Mercer. For illustrative purposes only. As at June 2024.

*Latest change made on 5 June 2024.

A constrained portfolio is one that is limited to core asset classes and cannot go underweight cash. Tracking error is the relative risk of the DAA positions. All assets are unhedged.

Global Property Market Outlook

- The first half of 2024 remains characterized by negative data points for property markets, but it is important to recognize that this is largely due to (1) the lagged nature of these data points and (2) the repricing occurring in the office sector which will take longer than other sectors.
- The summer months of 2024 appear to be the early days of market stabilization – when prices are still attractive, and negotiating power sits with capital providers. We therefore encourage investors not to be spooked by near-term noise but to focus on the medium-term opportunity and long-term benefits of a real estate allocation.
- Despite heightened political risk this year, the global economy remains broadly on course for a “soft landing”, supporting the strong occupational fundamentals in most real estate sectors and markets. It is important to recognise that positive rental growth and inflation-driven NOI growth softens the impact from outward yield shift and higher debt costs.
- Open-ended funds are reaching a historically low point in NAV, and some funds seem to have turned the corner. However, redemption queues in the US pose an uncertainty both to the market and for new investors. This notwithstanding, for the strongest funds, a low entry basis and shortened drawdown periods provide a good track record starting point. Without making stretched assumptions, managers are predicting double digit fund returns in the 2025 for low-risk real estate.
- For those clients with a higher risk appetite, the opportunity to achieve outsized returns from market dislocations also remains. Managers of value-add and opportunistic funds are seeing attractive repricing opportunities materialise and investors can best take advantage by committing capital to funds able to deploy in the near-term.
- As traditional banks retrench, re-financings mature and the funding gap grows, we also see the opportunity for alternative lenders to deploy capital and generate equity-like returns while occupying a sheltered position in the capital stack. However, with many US funds having raised significant capital, competition can be fierce, and margins have started to come down as managers compete for deals in sectors perceived to be most attractive (such as residential). This makes sourcing channels a critical factor to assess.
- Finally, over the longer term, real estate has the potential to provide asynchronized returns from liquid investments or other private market asset classes due to the asset class’s inflation-linked qualities and ability to tap into different economic sectors that can provide diversifier in terms of sources of return. This remains a fundamental reason to consider including the asset class in a diversified portfolio.

		EUROPE		
Equity		Core/ Core+	Value Add	Oppor- tunistic
	Themes	CPI Linkage	ESG refurb	Niche sectors
		Convenience Retail	Logistics Aggregation	Secondary locations
		Offices	High leverage	Spec Development

Attractive value: With the interest rate cycle on its descent, we have upgraded Europe core/core-plus to attractive after seven quarters at neutral or below. Demand for European core/core-plus real estate is tentatively returning as portfolio valuations look attractive from an historic perspective. Other regions should follow in time. Certain core/core-plus strategies such as US logistics already appear attractive value.

Worst value: We continue to be cautious on traditional value-add strategies which require high leverage and strong economic growth to hit target returns. Across risk levels, significant risks remain in the office sector which suffers from a significant drop in investor demand while traditionally making up a substantial part of investor portfolios.

Disclaimer: For illustration purposes only. The above table presents a simplified perspective at the time of writing this report and is subject to change without notice. All categories offer attractive opportunities and optimal allocations are subject to manager selection. The outlook represented is for new investors with a non-constrained risk budget over a 3-to-5-year investment horizon. 'Unattractive' positions therefore do not imply advice to liquidate existing investments.

Further guidance is available in Mercer's *Global Market Summary: Quarterly Real Estate Report, July 2024*



Summary of Mandates

Manager	Mandate	Benchmark/Target	Outperformance Target (p.a.)	Inception Date
BlackRock	Passive Paris-Aligned Equity (Synthetic Exposure)	MSCI Paris-Aligned Benchmark	-	May 2023
Brunel	Global High Alpha Equity	MSCI World	+2-3%	November 2019
Brunel	Global Sustainable Equity	MSCI AC World	+2%	September 2020
Brunel	Passive Global Equity Paris Aligned	FTSE Developed World PAB Index	-	October 2021
Brunel	Diversified Returns Fund	SONIA +3-5% p.a.	-	July 2020
Brunel	Multi-Asset Credit	SONIA +4-5% p.a.	-	June 2021
Brunel	UK Property	MSCI/AREF UK Quarterly Property Fund Index	-	January 2021
Partners	Overseas Property	Net IRR of 10% p.a. (local currency)	-	September 2009
Brunel	Secured Income (Cycles 1-3)	CPI	+2%	January 2019
IFM	Core Infrastructure	SONIA +5% p.a.	-	April 2016
Brunel	Renewable Infrastructure (Cycles 1-3)*	CPI	+4%	January 2019
Brunel	Private Debt (Cycles 2-3)	SONIA + 4% p.a.	-	September 2021
Schroders Greencoat	Wessex Gardens*	SONIA + 3% p.a.	-	February 2024
BlackRock	Buy-and-Maintain Corporate Bonds	Return on bonds held	-	February 2016
BlackRock	Matching (Liability Driven Investing)	Return on liabilities being hedged	-	February 2016
Record	Passive Currency Hedging	N/A	-	March 2016
BlackRock	Exchange-Traded Fund (ETF)	Bespoke benchmark to reflect total Fund allocation	-	March 2019
Cash	Internally Managed	-	-	-

* The primary performance objective for both of these mandates is a Net IRR of 8% p.a. (GBP). The inflation/cash-plus benchmarks are used by the custodian due to a greater ability to incorporate and the objective has value over the relative short-term, however, over time, comparison against the IRR objective will become more relevant.

Market Background Indices

Asset Class	Index
UK Equity	FTSE All-Share
Global Equity	FTSE All-World
Overseas Equity	FTSE World ex-UK
US Equity	FTSE USA
Europe (ex-UK) Equity	FTSE World Europe ex-UK
Japanese Equity	FTSE Japan
Asia Pacific (ex-Japan) Equity	FTSE World Asia Pacific ex-Japan
Emerging Markets Equity	FTSE Emerging
Global Small Cap Equity	MSCI World Small Cap
Sustainable Equity	MSCI World Low Carbon Target
Hedge Funds	HFRX Global Hedge Fund
High Yield Bonds	ICE BofAML Global High Yield
Emerging Market Debt	JP Morgan GBI EM Diversified Composite
Property	MSCI UK Monthly Total Return: All Property
Commodities	S&P GSCI
Over 15 Year Gilts	FTA UK Gilts 15+ year
Sterling Non Gilts	ICE BofAML Sterling Non Gilts
Over 5 Year Index-Linked Gilts	FTA UK Index Linked Gilts 5+ year
Global Bonds	ICE BofAML Global Broad Market
Global Credit	Bloomberg Capital Global Credit
Eurozone Government Bonds	ICE BofAML EMU Direct Government
Cash	SONIA

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